

Arts Academy in the Woods

Financial Report

June 30, 2003

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Arts Academy in the Woods

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Independent Auditor's Report

To the Board of Directors
Arts Academy in the Woods
Warren, Michigan

We have audited the accompanying general purpose financial statements of Arts Academy in the Woods as of and for the year ended June 30, 2003, as listed in the table of contents. Those general purpose financial statements are the responsibility of the management of Arts Academy in the Woods. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of Arts Academy in the Woods at June 30, 2003 and the results of its operations for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 25, 2003 on our consideration of Arts Academy in the Woods' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Plante & Moran, PLLC

September 25, 2003

Report Letter on Compliance with Laws and Regulations and Internal Control - General Purpose Financial Statements

To the Board of Directors
Arts Academy in the Woods
Warren, Michigan

We have audited the financial statements of Arts Academy in the Woods as of and for the year ended June 30, 2003 and have issued our report thereon dated September 25, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Arts Academy in the Woods' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*. Arts Academy in the Woods adopted a Special Revenue Fund budget deficit, which is not permissible under the Uniform Budgeting and Accounting Act. In addition, the Arts Academy in the Woods borrowed monies during the 2003 fiscal year prior to receiving qualified status with the Michigan Department of Treasury or obtaining permission from the Michigan Department of Treasury as required under the Revised Municipal Finance Act.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Arts Academy in the Woods' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the Academy's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

To the Board of Directors
Arts Academy in the Woods

Management oversight and review are integral components of the Academy's internal control structure. Adequate review of the Academy's revenue and expenditure activity as well as year-end balances of asset and liability accounts was not performed on a timely basis during the year, which resulted in unplanned expenditures and additional journal entries subsequent to year end.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. However, we believe the reportable conditions described above are not material weaknesses.

This report is intended for the information of the Board of Directors and management and is not intended to be and should not be used by anyone other than these specified parties.

Plante & Moran, PLLC

September 25, 2003

Arts Academy in the Woods

Combined Balance Sheet Governmental Fund Types and Account Group June 30, 2003

	Governmental Fund Types		General Fixed Assets
	Special		Account
	General	Revenue	Group
Assets			
Cash and cash equivalents (Note 3)	\$ 82,865	\$ 3,493	\$ -
Accounts receivable	-	2,041	-
Due from other funds	27,463	-	-
Due from other governmental units	217,365	-	-
Inventories	-	1,313	-
Property and equipment (Note 5)	-	-	134,727
Total assets	<u>\$ 327,693</u>	<u>\$ 6,847</u>	<u>\$ 134,727</u>
Liabilities, Fund Equity (Deficit), and Other Credits			
Liabilities			
Accrued liabilities	\$ 106,243	\$ 1,416	\$ -
Deferred revenue	13,294	-	-
Due to other funds	-	27,463	-
Due to other governmental units	372,087	-	-
Total liabilities	491,624	28,879	-
Fund Equity (Deficit) and Other Credits			
Investment in general fixed assets	-	-	134,727
Fund balance (deficit):			
Reserved for inventories	-	1,313	-
Unreserved and undesignated	(163,931)	(23,345)	-
Total fund equity (deficit) and other credits	<u>(163,931)</u>	<u>(22,032)</u>	<u>134,727</u>
Total liabilities, fund equity (deficit), and other credits	<u>\$ 327,693</u>	<u>\$ 6,847</u>	<u>\$ 134,727</u>

Arts Academy in the Woods

Statement of Revenue, Expenditures, and Changes in Fund Balances - All Governmental Fund Types Year Ended June 30, 2003

	General Fund	Special Revenue Fund
Revenue		
Local sources	\$ 2,082	\$ 31,512
State sources	1,122,642	70
Federal sources	220,211	14,786
Total revenue	1,344,935	46,368
Expenditures - Current		
Instruction	906,876	-
Support services:		
Guidance services	4,575	-
Library	4,225	-
Board of Education	9,277	-
Executive administration	120,300	-
Office of principal	66,738	-
Business services	347,077	-
Operation and maintenance	64,480	-
Food services	-	60,336
Total expenditures	1,523,548	60,336
Excess of Expenditures Over Revenue	(178,613)	(13,968)
Fund Balances (Deficits) - Beginning of year	14,682	(8,064)
Fund Deficits - End of year	<u>\$ (163,931)</u>	<u>\$ (22,032)</u>

Arts Academy in the Woods

General Fund Statement of Revenue, Expenditures, and Changes in Fund Balance - Budget and Actual Year Ended June 30, 2003

	Budget	Actual	Over (Under) Budget
Revenue			
Local sources	\$ 185,900	\$ 2,082	\$ (183,818)
State sources	1,213,364	1,122,642	(90,722)
Federal sources	222,380	220,211	(2,169)
Total revenue	1,621,644	1,344,935	(276,709)
Expenditures			
Instruction:	953,007	906,876	(46,131)
Support services:			
Guidance services	-	4,575	4,575
Library	2,500	4,225	1,725
Board of Education	14,500	9,277	(5,223)
Executive administration	147,884	120,300	(27,584)
Building administration	265,565	243,160	(22,405)
Operations and maintenance	67,404	64,480	(2,924)
Business services	169,000	170,655	1,655
Total support services	666,853	616,672	(50,181)
Total expenditures	1,619,860	1,523,548	(96,312)
Excess of Revenue Over (Under) Expenditures	1,784	(178,613)	(180,397)
Fund Balance - Beginning of year	14,682	14,682	-
Fund Balance (Deficit) - End of year	<u>\$ 16,466</u>	<u>\$ (163,931)</u>	<u>\$ (180,397)</u>

Arts Academy in the Woods

Special Revenue Fund Statement of Revenue, Expenditures, and Changes in Fund Balance - Budget and Actual Year Ended June 30, 2003

	Budget	Actual	Over (Under) Budget
Revenue			
Local sources	\$ 32,000	\$ 31,512	\$ (488)
State sources	-	70	70
Federal sources	<u>11,000</u>	<u>14,786</u>	<u>3,786</u>
Total revenue	43,000	46,368	3,368
Expenditures			
Salaries	19,600	23,870	4,270
Benefits	7,600	12,624	5,024
Supplies and other	26,655	23,401	(3,254)
Capital outlay	<u>18,000</u>	<u>441</u>	<u>(17,559)</u>
Total expenditures	<u>71,855</u>	<u>60,336</u>	<u>(11,519)</u>
Excess of Expenditures Over Revenue	(28,855)	(13,968)	14,887
Fund Deficit - Beginning of year	<u>(8,064)</u>	<u>(8,064)</u>	-
Fund Deficit - End of year	<u><u>\$ (36,919)</u></u>	<u><u>\$ (22,032)</u></u>	<u><u>\$ 14,887</u></u>

Arts Academy in the Woods

Notes to Financial Statements
June 30, 2003

Note 1 - Summary of Significant Accounting Policies

The accounting policies of Arts Academy in the Woods (the "Academy") conform to accounting principles generally accepted in the United States of America as applicable to public school academies. The following is a summary of the significant accounting policies:

Reporting Entity

The Academy was formed as a public school academy pursuant to the Michigan School Code of 1976, as amended by Act No. 362 of the Public Acts of 1993 and Act No. 416 of the Public Acts of 1994.

On November 10, 2000, the Academy entered into a five-year contract with Macomb Intermediate School District (MISD) to charter a public school academy. The contract requires the Academy to act exclusively as a governmental agency and not undertake any action inconsistent with its status as an entity authorized to receive State school aid funds pursuant to the State Constitution. Warren Woods Public Schools is the fiscal agent for the Academy and is responsible for overseeing the Academy's compliance with the contract and all applicable laws. The Academy pays 10 percent of its State aid as administrative fees to Warren Woods Public Schools. The total administrative fee paid for the year ended June 30, 2003 was \$114,294.

The accompanying general purpose financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational or financial relationships with the public school academy. Based on application of the criteria, the entity does not contain component units.

Fund Accounting

The accounts of the Academy are organized on the basis of funds and an account group, each of which is considered a separate accounting entity. The Academy maintains two governmental funds, the General Fund and the Special Revenue Fund. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund balance, revenue, and expenditures.

Governmental Funds

Governmental funds are those funds through which most public school academy functions typically are financed. The acquisition, use, and balances of the Academy's expendable financial resources and the related current liabilities are accounted for through a governmental fund.

Arts Academy in the Woods

Notes to Financial Statements June 30, 2003

Note 1 - Summary of Significant Accounting Policies (Continued)

General Fund - The General Fund is used to record the general operations of the Academy pertaining to education and supporting operations. Included are all transactions related to the approved current operating budget.

Special Revenue Fund - The Special Revenue Fund is used to account for the proceeds of specific revenue sources that are restricted to expenditure for specified purposes. Any deficit generated by this fund is the responsibility of the General Fund.

Account Group - An account group is not a fund - it does not reflect available financial resources and related liabilities or the measurement of results of operations - but is the Academy's accounting records of general fixed assets. The General Fixed Assets Account Group is used to maintain records of the cost of building improvements, furniture, and equipment owned by the Academy.

Basis of Accounting

The funds utilize the modified accrual basis of accounting. Modifications in such method from the accrual basis are as follows:

- a. Revenue that is both measurable and available for use to finance operations is recorded as revenue when earned. Other revenue is recorded when received.
- b. Payments for inventorable types of supplies, which are not significant at year end, are recorded as expenditures at the time of purchase.
- c. Revenue from State sources is primarily governed by the School Aid Act and the School Code of Michigan. The State of Michigan utilizes a foundation allowance funding approach, which provides for a specific annual amount of State revenue per student. The foundation allowance is provided from the State's School Aid Fund and is recognized as revenue in accordance with State law.

General Fixed Assets - General fixed assets are recorded as expenditures in the governmental fund in the year payment is made or expenditure accrued. Such assets are recorded at cost or, if donated, at their estimated fair value on the date donated in the General Fixed Assets Account Group.

Arts Academy in the Woods

Notes to Financial Statements June 30, 2003

Note 2 - Budgets

Budgetary Information - The Academy formally adopted a General Fund and Special Revenue Fund line-item budget for the year ended June 30, 2003. Expenditures at this level in excess of amounts budgeted are a violation of Michigan law. Unexpended appropriations lapse at year end; encumbrances are not included as expenditures. The amount of encumbrances outstanding at June 30, 2003 is unknown. During the year ended June 30, 2003, the budget was amended in a legally permissible manner with the exception of adopting a budget deficit in the Special Revenue Fund. The budget amounts reflected in the General Fund and Special Revenue Fund statement of revenue, expenditures, and changes in fund balance - budget and actual are a summarization of the Academy's line-item adopted budget, presented in conformity with generally accepted accounting principles. A comparison of actual revenue and expenditures to the adopted budget is available for inspection at the Academy's offices.

Fund Deficits/Deficit Elimination Plan - The Academy has an accumulated fund balance deficit in the General Fund and the Special Revenue Fund in the amounts of \$163,931 and \$22,032, respectively. The Academy's plans to eliminate the deficits include:

- Increased pupil count in fiscal year 2003-2004, resulting in additional revenue
- Detail review of budgeted expenditures, including service provider fees
- Evaluation of food services program by an outside consultant for recommendations to increase profitability
- Salary and wage freeze

Note 3 - Deposits and Investments

The Academy's cash and cash equivalents at June 30, 2003 consisted of the following:

Deposits	\$ 86,043
Investments	<u>315</u>
Total	<u>\$ 86,358</u>

The deposits were reflected in the accounts of the bank (without recognition of checks written but not yet cleared or of deposits in transit) at \$117,183, all of which was covered by federal depository insurance.

Arts Academy in the Woods

Notes to Financial Statements June 30, 2003

Note 3 - Deposits and Investments (Continued)

Investments

The Academy is authorized by Michigan Public Act 132 of 1986 to invest surplus monies in U.S. bonds and notes, certain commercial paper, U.S. government repurchase agreements, bankers' acceptances and mutual funds, and investment pools that are composed of authorized investment vehicles.

The Academy's investments at year end were entirely invested in interlocal agreement investment pools that had a carrying amount of \$315.

Investments are normally categorized to give an indication of the level of risk assumed by the Academy; however, cash management funds, which include interlocal agreement investment pools, are not categorized because they are not evidenced by securities that exist in physical or book entry form. Management believes the investments in the funds comply with the investment authority noted above.

Note 4 - Defined Benefit Pension Plan

Plan Description - The Academy participates in the Michigan Public School Employees' Retirement System (MPSERS), a statewide, cost-sharing, multiple-employer defined benefit public employee retirement system governed by the State of Michigan that covers substantially all employees of the Academy. The MPSERS provides retirement, survivor, and disability benefits to plan members and their beneficiaries. The MPSERS issues a publicly available financial report that includes financial statements and required supplementary information for the MPSERS. That report may be obtained by writing to the MPSERS at 7150 Harris Drive, P.O. Box 30673, Lansing, MI 48909-8103.

Funding Policy - Employer contributions to the MPSERS result from the implementing effects of the School Finance Reform Act. Under these procedures, each school district is required to contribute the full actuarial funding contribution amount to fund pension benefits, plus an additional amount to fund retiree health care benefit amounts on a cash disbursement basis. The pension benefit rate totals 12.17 percent for the period from July 1, 2002 through September 30, 2002 and 12.99 percent for the period from October 1, 2002 through June 30, 2003 of the covered payroll to the plan. Basic plan members make no contributions, but may contribute to a Member Investment Plan (MIP) at rates ranging from 3 percent to 4.3 percent of gross wages. The Academy's contributions to the MPSERS plan for the years ended June 30, 2003 and 2002 was \$82,767 and \$65,559, respectively.

Arts Academy in the Woods

Notes to Financial Statements June 30, 2003

Note 4 - Defined Benefit Pension Plan (Continued)

Postemployment Benefits - Under the MPSERS Act, all retirees participating in the MPSERS pension plan have the option of continuing health, dental, and vision coverages. Retirees having these coverages contribute an amount equivalent to the monthly cost for Part B Medicare and 10 percent of the monthly premium amount for the health, dental, and vision coverages. Required contributions for postemployment health care benefits are included as part of the Academy's total contribution to the MPSERS plan discussed above.

Note 5 - General Fixed Assets

The balances of the general fixed assets as of June 30, 2003 are as follows:

Building improvements	\$ 5,260
Machinery, equipment, and furniture	<u>129,467</u>
Total	<u>\$ 134,727</u>

Note 6 - Risk Management

The Academy is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Academy has purchased commercial insurance for all claims. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage since inception.

Note 7 - Related Party

The Academy has a lease agreement with its acting fiscal agent, Warren Woods Public Schools, for certain property. The required monthly payments of the lease from July 2002 through August 2002 totaled \$10,000, and from September 2002 through June 2003 totaled \$12,500. Rent expense related to this lease totaled \$145,000 for the year ended June 30, 2003.

In addition, the Arts Academy in the Woods borrowed funds from Warren Woods Public Schools during the 2003 fiscal year prior to receiving qualified status with the Michigan Department of Treasury or obtaining permission from the Michigan Department of Treasury as required under the Revised Municipal Finance Act.

Arts Academy in the Woods

Notes to Financial Statements June 30, 2003

Note 8 - Subsequent Event

On August 21, 2003, the Academy borrowed \$520,000 at 3.25 percent annual interest on a tax anticipation note (State Aid Anticipation Note). The note, plus interest, is due in August 2004, which will be automatically deducted in equal monthly installments from October 2003 through August 2004.

Note 9 - Upcoming Reporting Change

For the year beginning July 1, 2003, the Academy plans to adopt GASB Statement No. 34. This will dramatically revise the information being reported in these financial statements. Governmental activities will report information by significant fund, as well as in total on the full accrual basis of accounting. Information is not available to present pro forma data that would show the effect of this future change.